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No. 95-1063

IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

WILLIAM B. BLOUNT,
Petitioner,
v.
SECURITIES AND EXCHANGE COMMISSION,
and
MUNICIPAL SECURITIES RULEMAKING BOARD,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

RESPONDENT MUNICIPAL SECURITIES RULEMAKING BOARD'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether Municipal Securities Rulemaking Board Rule G-37, which prohibits those engaged in municipal securities business from doing business with issuers to whose officials they have made contributions, and from soliciting contributions for officials of issuers with whom they do or seek to do business, violates the First Amendment, when the Rule is narrowly tailored to curb the risk and appearance of corruption and coercion in the municipal securities industry, while leaving those in the municipal securities business free to engage in a vast array of political activities on behalf of these or any other officials, candidates, or causes.

2. Whether Municipal Securities Rulemaking Board Rule G-37, which does not regulate state or local elections but rather the conduct of persons and entities seeking to participate in interstate trade in municipal securities, violates the Tenth Amendment.

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RESPONDENT MUNICIPAL SECURITIES RULEMAKING BOARD'S BRIEF IN OPPOSITION

COUNTERSTATEMENT

In recent years, there has been increasing concern that brokers, dealers, and municipal securities dealers (collectively, "dealers"),[1] along with municipal issuers, were involved in certain ethically questionable practices, known colloquially as "pay-to-play." Specifically, it was widely reported that dealers were able to enhance their prospects

[1] Under the Securities Exchange Act of 1934, "broker," "dealer," and "municipal securities dealer" all have particularized definitions, but in general refer to persons or entities engaged in the business of effecting securities transactions. *See* 15 U.S.C. §§ 78c(a)(4), (5), and (30).

of securing lucrative municipal securities contracts from government issuers by making campaign contributions to public officials of those issuers. More precisely defined, "pay-to-play" means that such campaign contributions are deemed a prerequisite to any serious consideration of the contributor to be awarded a given issuer's securities business. Although the contribution would not guarantee such business (because many potential dealers might make such contributions), it was a precondition—or at least an aid—in securing it.

To address the issues associated with pay-to-play, the Municipal Securities Rulemaking Board ("MSRB") proposed and filed Rule G-37 with the Securities and Exchange Commission ("SEC"), which the SEC ultimately approved. Rule G-37 generally prohibits those engaged in the municipal securities business from doing business for two years with issuers to whose officials they have made campaign contributions, and from soliciting such contributions for officials of issuers with whom they do or seek to do business.[2] A unanimous panel of the District of Columbia Circuit, in a thorough and well-reasoned decision authored by Judge Stephen F. Williams, concluded that Rule G-37 fell well within the permissible boundaries of this Court's First and Tenth Amendment precedent, and rejected petitioner's First and Tenth Amendment challenges to the Rule. *Blount v. SEC*, 61 F.3d 938 (D.C. Cir. 1995).

A. The MSRB

Congress established the MSRB in 1975 to develop rules for governance of the municipal securities industry. 15 U.S.C. § 78o-4(b). The MSRB is a not-for-profit, non-stock corporation, specifically designated as a "self-regulatory organization" under the Securities Exchange

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[2] The Rule's definition of issuer officials specifically includes candidates for office of such issuers.

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Act of 1934.[3] The MSRB consists of fifteen members, ten of whom are themselves "associated with and representative of" municipal securities brokers and dealers. Five of the members are "public representatives" not associated with any municipal securities dealer. Those five must include at least one representative of investors in municipal securities, and one representative of municipal securities issuers (*e.g.*, state and local governments). *Id.* Because of its composition, the MSRB has an unusually well-balanced and realistic view of the issues affecting municipal securities markets and the conduct of dealers in those markets.

Congress specifically charged the MSRB with responsibility for developing rules to:

- Prevent fraudulent and manipulative acts and practices.
- Promote just and equitable principles of trade.
- Remove impediments to, and perfect the mechanism of, a free and open market in municipal securities.
- Protect investors and the public interest.

Id. at § 78o-4(b)(2)(C). Following this mandate, the MSRB has proposed, and the SEC has ultimately approved, rules governing the activities, obligations, and responsibilities of dealers, including the rule at issue in this case.

MSRB rules generally do not take effect unless and until the SEC approves them. Before submitting a rule to the SEC for approval, the MSRB typically provides a notice and comment period during which it receives and considers comments on the proposed rule, and revises the

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[3] As defined by the Act, a "self-regulatory organization" is "any national securities exchange, registered securities association, or registered clearing agency," and specifically includes the MSRB. 15 U.S.C. § 78c(a)(26).

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rule accordingly. Once the proposed rule is filed with the SEC, the SEC itself seeks comments. After considering the comments, the SEC will approve a proposed MSRB rule only if it concludes that the rule is consistent with the purposes of the Securities Exchange Act (*id.* at § 78(s)) and all other applicable law.

B. Pay-to-Play

Municipal securities are securities issued by states and their political subdivisions. They are generally employed to help finance a wide range of public projects, including roads, bridges, schools, hospitals, water and sewer projects, and countless other projects meant for the public good. Upon issuance, the securities are generally sold to dealers, who may then resell the securities to the public at a profit. The municipal securities market is enormous: there are 1.3 million municipal securities issues outstanding, with a value of over $1.2 trillion.

The municipal securities industry is unique in one respect. Municipal securities are, by definition, issued by government entities. This often means that the issuer's officials are subject to election, and thus subject to the economic pressures created by modern electoral politics. In the absence of regulation, dealers might well be in a position to provide substantial sums of money—through campaign contributions or solicitations—to the very government officials who will decide or who may influence the decision whether those dealers are to be awarded potentially lucrative municipal securities contracts.

The temptations on both sides are obvious. Government officials need campaign contributions to get to and stay in office. The dealer is seen as a source of funds and access to further sources of funds from other participants in the financial markets. For their part, dealers can profit greatly by securing the municipal securities contracts for certain municipal issues.

Historically, municipal financing contracts were awarded through a competitive bidding process, generally based on price. *SEC Approval Order* at Appendix to Petition ["App."] at B-6 and B-6 n.11. In recent years, however, more and more issuers have replaced the competitive bidding process with "negotiated underwritings," in which the issuer leaves itself with considerable leeway to choose the dealer based on subjective judgments. The process has fueled concern that dealers are being chosen *not* on the basis of price or merit, but rather based on other, "non-merits" considerations. *Id.* at App. B-6 to B-9. Hence, the concern with pay-to-play, wherein dealers must "pay" (*i.e.*, contribute or solicit contributions to political campaigns) in order to "play" (*i.e.*, to be considered for municipal securities business).

The idea that campaign contributions could influence the choice of dealer in this setting is as easily understood as it is pervasive. (Indeed, how could contributions *not* influence that choice?) Petitioner himself, a municipal bond dealer, candidly acknowledged the kind of linkage between well-placed contributions and the award of municipal securities business that the Rule is meant to combat: "most likely [state and local officials] are gonna call somebody who has been a political contributor" and award contracts to "friends" who have been contributors. Interview with William B. Blount, *Morning Edition* (National Public Radio, June 1, 1994), *available in* LEXIS, News Library, Transcript No. 1358-9; *see Blount*, 61 F.3d at 945.

Reports of pay-to-play practices burgeoned in the 1980's and early 1990's, with some dealers coming to regard pay-to-play as an ordinary cost of seeking business from certain municipal issuers. The integrity of the municipal securities market, and the integrity of the business practices used to obtain municipal securities business, were widely questioned. *SEC Approval Order* at App. at B-9 to B-13.

C. Rule G-37

Since 1990, the MSRB has monitored, considered, and publicly discussed the pay-to-play problem. While the MSRB initially urged industry members to voluntarily curb pay-to-play practices, it became increasingly convinced that a rule was necessary to adequately address the pay-to-play problem. In August 1993, MSRB published a draft rule on contributions. After revising the draft in light of some of the comments it received, the MSRB submitted Rule G-37 to the SEC, which in turn initiated its own notice and comment period in January 1994. On April 7, 1994, after the close of the comment period, the SEC issued an order approving the rule. (*See* App. B).

Petitioner challenges subsections (b) and (c) of the Rule. Subsection (b) bars any dealer from "engag[ing] in municipal securities business with an issuer within two years after any contribution to an official of such issuer made by" the dealer or by "any municipal finance professional asociated with" the dealer.[4] The two-year prohibition is not triggered, however, by total contributions of $250 or less per official per election to an official for whom the municipal finance professional is entitled to vote.

The MSRB added subsection (c) to the Rule after commentors observed that subsection (b)'s business prohibition could easily be evaded by soliciting or coordinating contributions for an official (a practice sometimes referred to as "bundling" contributions).[5] Subsection (c)

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[4] Under Rule G-37, a "municipal finance professional" generally refers to an associated person who solicits, supervises, or engages in the dealer's municipal securities business. *See* Rule G-37(g)(iv). The Rule also bars the dealer from doing business with an issuer for a period of two years if a political action committee controlled by the dealer contributes to an official of that issuer (*id.* at (b)(iii)), although this provision of the rule is not at issue in this case.

[5] Petitioner's assertion that subsection (c) was added by the MSRB "as an afterthought . . . with no explanation whatsoever

therefore prohibits any dealer—and any municipal finance professional of the dealer—from soliciting or coordinating contributions for officials of any issuer with whom the dealer is "engaging or is seeking to engage in municipal securities business."[6]

In drafting and approving Rule G-37, the MSRB and SEC were sensitive to First Amendment concerns. *See SEC Approval Order* at App. B-34 to B-40. The Rule is limited in time, scope, and reach. It applies only to dealers and municipal finance professionals who do or seek to do business with the same issuers to whose officials they have made or solicited contributions. Even within that limited context, the Rule applies only to negotiated business; it does not apply to competitive bidding. *Id.* at B-18 n.41.

Moreover, the Rule applies *only* to the making or soliciting of campaign *contributions*—the giving of money directly to candidates or their campaigns. The Rule does *not* apply to *independent expenditures*—*i.e.*, expenditures in support of a candidate which are uncontrolled and uncoordinated by the candidate or campaign.[7] Thus, the

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of the reason or need for it" (Petition at 5) is simply untrue. *See* MSRB Statement of the Purpose for the Proposed Rule Change, JA 652-53, 657. (JA refers to the Joint Appendix filed in the Court of Appeals and containing the record on review.)

[6] Subsections (b) and (c) are supplemented by subsection (d), a "loophole closing" provision which prohibits dealers from "directly or indirectly" doing anything that would "result in a violation of sections (b) or (c) . . . ." While petitioner mounted a "vagueness" challenge to subsection (d) in the Court of Appeals (*see* 61 F.3d at 948-49), he apparently abandons that challenge here. Subsections (b), (c), and (d) to Rule G-37 are set forth in their entirety in Appendix G to the Petition. The complete Rule is set forth at JA 644-50.

[7] *See Buckley v. Valeo*, 424 U.S. 1, 48-49 (1976). As defined by federal election law, an "independent expenditure" means "an expenditure by a person expressly advocating the election or defeat of a clearly identified candidate which is made without cooperation

Rule has no effect whatever on dealers' or municipal finance professionals' spending as much money as they want on behalf of any candidate, so long as the expenditures are not coordinated with or controlled by the candidate or campaign. Nor does the Rule limit the ability of dealers or municipal finance professionals to make speeches, attend fundraising events, or otherwise engage in the vast majority of political activities on behalf of the officials with whom they do business—or for that matter, on behalf of any other candidate or cause.

D. The Decision Below

Petitioner sought review of the SEC's order approving Rule G-37 in the United States Court of Appeals for the District of Columbia Circuit. On August 4, 1995, a unanimous panel of that court (Judge Williams, writing for himself, Judge Henderson and Judge Rogers) rejected petitioner's challenge after carefully considering each of petitioner's First and Tenth Amendment arguments (many of which are not repeated in the Petition to this Court). 61 F.3d 938.[8]

The court approached the First Amendment argument by analyzing Rule G-37 within the framework of this Court's well-established precedent for judging restrictions that affect the making and soliciting of campaign contributions, particularly as set forth in *Buckley v. Valeo*, 424 U.S. 1 (1976) and its progeny. It thus began by considering the level of First Amendment scrutiny to apply to Rule G-37. Finding no "clear-cut" guidance in this Court's cases on that issue, the court reasoned that "[i]f the rule can withstand strict scrutiny, there is no

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or consultation with any canididate, or any authorized committee or agent of such candidate, and which is not made in concert with, or at the request or suggestion of, any candidate, or any authorized committee or agent of such candidate." 2 U.S.C. § 431(17).

[8] The circuit court rejected petitioner's petition for rehearing and suggestion for rehearing en banc on October 4, 1995.

need to decide the issue" (*id.* at 943); thus, the "level-of-scrutiny" issue was not resolved. Rather, following the paradigm for "strict scrutiny" review employed by this Court in similar cases, it held that the Rule survives even the strictest First Amendment scrutiny.[9]

First, the Court of Appeals recognized the governmental and regulatory interest furthered by Rule G-37—protecting the municipal securities industry from the risk and appearance of unfair and corrupt market practices—was both "substantial" and "compelling." *Id.* at 944.[10]

Second, the Court of Appeals held that "the provisions of Rule G-37 at issue can be expected materially to advance compelling interests asserted" by the government. *Id.* at 946. Specifically, the court found that in an industry in which dealers can make or solicit contributions to the same officials who decide whether to award them municipal securities business, the risk and appearance of both corruption and coercion is "obvious and substantial." *Id.* at 945. The court also recognized the obvious link between eliminating pay-to-play practices (under which dealers are considered for business not on the basis of merit, but based on the contributions they have made or solicited) and the goals of "perfecting the mechanism of a free and open market" and promoting "just and equitable principles of trade." *Id.*

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[9] The MSRB believes that Rule G-37 does not focus on the content of speech and is thus not subject to strict scrutiny. However, MSRB also agrees with the Court of Appeals that since Rule G-37 survives strict as well as intermediate scrutiny, the issue is immaterial.

[10] The court found that a second interest proffered to support Rule G-37—protecting investors in municipal bonds from fraud—was also substantial and compelling. The court concluded, however, that the Rule did not sufficiently advance that interest to survive strict scrutiny. *See id.* at 945. While MSRB disagrees with this aspect of the court's ruling, it is immaterial for purposes of Blount's petition to this Court. The interest in market integrity identified by the court was clearly sufficient to justify the Rule.

Finally, the court held that Rule G-37 is narrowly tailored, *i.e.*, "closely drawn" and "avoid[s] unnecessary abridgement" of First Amendment rights. *Id.* at 947 (quoting *Buckley v. Valeo*, 424 U.S. at 25). The court rejected petitioner's argument that the Rule's solicitation provision was unnecessary. The court recognized that the Rule's business prohibition, standing alone, could easily be evaded by soliciting or coordinating contributions, thus necessitating restrictions on those activities. The court rejected petitioner's further argument that the Rule's goals could have been achieved through the less restrictive alternatives presented by disclosure requirements. The court held that disclosure and record-keeping alone would not provide an effective check in a situation where contributions are exchanged not for guaranteed business, but rather for the opportunity to be considered for business. *Id.* at 947.

The court found that Rule G-37 was limited in scope and effect. The Rule constrains relations only between the two potential parties to a *quid pro quo*: dealers on the one hand, and the officials who might influence the award of negotiated municipal securities contracts on the other. The Rule applies *only* to negotiated business (and not to competitive bid contracts), and even then restricts a narrow range of activities for a relatively short amount of time. *Id.* The court observed further that dealers and municipal finance professionals are "not in any way restricted from engaging in the vast majority of political activities, including making direct expenditures for the expression of their views, giving speeches, soliciting votes, writing books, or appearing at fundraising events." *Id.* at 948. Accordingly, the court held that Rule G-37 withstands even the strictest First Amendment scrutiny.

The Court of Appeals also rejected petitioner's Tenth Amendment claim that Rule G-37 usurps the power of States to control municipal or state elections. The court saw no basis for petitioner's effort to characterize the prohibitions as a federal agency effort to regulate local

elections: Rule G-37 is directed specifically at the conduct of persons who seek to participate in interstate trade in municipal securities. Nothing in the Tenth Amendment prohibits the federal government from regulating the conduct of private parties, irrespective of the fact that such conduct may affect local government (or local elections). That court thus concluded that petitioner's Tenth Amendment claim was "meritless." *Id.* at 949.

REASONS FOR DENYING THE WRIT

The petition raises neither a novel constitutional question nor an issue upon which the courts of appeal are divided. To the contrary, both the First Amendment and the Tenth Amendment arguments are foreclosed by long-standing precedent of this Court. In addition, this case is unrelated to *FEC v. Colorado Republican Campaign Committee*, 59 F.3d 1015 (10th Cir. 1995), *cert. granted*, 116 S. Ct. 689 (Jan. 5, 1996), which involves restrictions imposed by the Federal Election Campaign Act ("FECA") on *political party expenditures*, which are of course distinguished from limitations affecting contributions by individuals. Indeed, the Court in *Buckley v. Valeo* expressly reserved the question whether FECA's limitations on political party expenditures violated the First Amendment, while at the same time holding that FECA's limitations on individual contributions do not. 424 U.S. 1, 24-29, 59 n.69 (1976).[11]

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[11] Nor is this case like *Carver v. Nixon*, 72 F.3d 633 (8th Cir. 1995), *petition for cert. filed* (Feb. 7, 1996). In *Carver*, the Eighth Circuit struck down a voter initiative imposing ceilings on individual campaign contributions which were lower than those provided for in an already existing (and still valid) statute. Whereas *Carver* involves direct and broad regulation of the electoral process for *all* citizens, Rule G-37 is a business regulation that applies only to those select individuals and entities which do or seek to do municipal securities business with issuers to whose officials they have made or solicited campaign contributions.

I. THE DISTRICT OF COLUMBIA CIRCUIT'S DECISION IS ENTIRELY CONSISTENT WITH *BUCKLEY v. VALEO* AND THE COURT'S OTHER FIRST AMENDMENT PRECEDENT.

1. There is nothing novel about governmental efforts to prevent corruption and corrupting practices—particularly, the potentially corrupting practices associated with giving money to decisionmakers—even though those practices arise in connection with political campaigns. Indeed, the Rule's restrictions are in all respects more modest and focused than many similar restrictions upheld by this Court, notwithstanding far more substantial and pervasive intrusions on First Amendment interests. In *Buckley v. Valeo*, the Court sustained the restrictions imposed by FECA on campaign *contributions* that *any* citizen may make in connection with federal elections, finding these to be warranted by the government's compelling need to avoid corruption, the appearance of corruption, and undue influence in connection with government action. The Court subsequently upheld FECA's restrictions on campaign *solictations* by corporations and labor unions.[12] And these types of restrictions have strong historic precedent in the federal government's absolute bar on contributions—along with gifts or gratuities to government officials—by those who seek government contracts. The Court has also upheld the Hatch Act's prohibition on federal employees—and state and local employees engaged in activities financed by federal funds—from taking *any* active part in political management or in political campaigns.[13] In sustaining such restrictions, this Court has reaffirmed that narrowly-tailored restrictions on participation in *certain* political campaign activities are justified by a compelling government interest

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[12] *FEC v. National Right to Work Comm.*, 459 U.S. 197 (1982).

[13] *United States Civil Service Comm'n v. National Ass'n of Letter Carriers*, 413 U.S. 548 (1973); *Oklahoma v. United States Civil Service Comm'n*, 330 U.S. 127 (1947).

in preventing the risk and appearance of corruption or coercion.

2. "Pay-to-play" clearly poses the risk and appearance of corruption and coercion in the municipal securities market. First, there is *corruption*: *i.e.*, that government officials will choose dealers not for the quality or price of their services, but for the size of the campaign contributions they have made or solicited, undermining the basic market foundational principle of competition on the merits. Second, there is *coercion*: *i.e.*, when pay-to-play practices are viewed as prevalent throughout the market, dealers are necessarily pressured to make contributions to, or solicit contributions for, officials (even if they *disagree* with them politically) because of the belief that such contributions are a precondition to obtaining government business. Those dealers who succumb to that pressure necessarily have participated in a "tainted practice"—undermining the ethical standards of those dealers. If some dealers choose not to compete (believing that a distasteful contribution is a prerequisite to consideration) —or if some dealers choose not to contribute (and such a contribution is indeed a prerequisite to consideration) —there will be fewer competitors, and competition in the market will suffer. Each of these evils affects the market and undermines the ethical foundations upon which the market, and those competing within the market, should operate.

Once prevalent, such "pay-to-play" practices are difficult to curb voluntarily, for candidates may come to depend on contributions from dealers to finance their campaigns. Thus, voluntary efforts on the part of dealers to curb pay-to-play practices were reportedly met with threats of boycotts by municipal securities issuers. *See, e.g.*, "Politicians Are Mobilizing To Derail Ban on Muni Underwriters," *Wall Street Journal*, Dec. 17, 1993, at C16 (reporting that Florida Association of Counties called for boycott of 17 firms that had voluntarily banned political contributions).

3. The Rule eliminates, of course, the risk and appearance of impropriety inherent in the receipt of lucrative contracts from the offices of public officials to whose campaign coffers money has been given or solicited. On its face, G-37 eliminates the potential for a *quid pro quo* in the form of an award of government business in exchange either for a campaign contribution, or assistance in obtaining contributions. But there is more to "perfecting the mechanism of a free and open market" and "promoting just and equitable principles of trade" (*see Blount*, 61 F.3d at 945) than eliminating the explicit or implicit *quid pro quo*. Rule G-37 also eliminates the risk and appearance that more subtle, but equally insidious, forms of "influence" (*e.g.*, access and preferential treatment) will govern the placing of municipal securities business. By eliminating these more subtle forms of "influence," it reinforces both the reality, and the perception, that competition for municipal securities business is being conducted "on the merits."

Similar to the concerns underlying the Hatch Act, Rule G-37 also seeks to ensure that dealers are "free from pressure and from express and tacit invitations to . . . perform political chores in order to curry favor . . . ." *United States Civil Service Comm'n v. National Ass'n of Letter Carriers*, 413 U.S. 548, 566 (1973). The Rule also ensures that those dealers who would choose not to or be unable to make or solicit contributions are not thereby foreclosed from certain municipal securities business, which would dilute a fair, open, and competitive market.[14]

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[14] In this respect, Rule G-37 *advances* First Amendment values by protecting dealers' "rights, notably their right to free expression, rather than restrict[ing] those rights." *United States v. National Treasury Employees Union*, 115 S. Ct. 1003, 1015 (1995). Protecting the First Amendment rights of dealers in this context is—for the reasons set forth above—perfectly consistent with protecting competition in the marketplace.

The Rule thus reinforces professional ethical standards of conduct by preventing dealers from benefitting from ethically questionable practices—or from being punished by declining to participate in such practices. It maintains honesty and integrity in the market and reaffirms the significant values associated with the belief that market forces—honest competition on the merits, rather than political influence—are and will be the guiding forces in the choice of dealers. There is a compelling government interest in all of these concerns.

4. While a Rule that touches upon political campaigns clearly has First Amendment implications, the Rule does not, of course, directly prohibit any First Amendment protected activity. Notwithstanding petitioner's effort to characterize the Rule as some sort of general effort by the SEC to regulate political campaigns (*see* Petition at 11), the Rule's focus is not on elections but on the municipal securities industry. At its core, it is an effort to monitor and supervise an interstate, commercial market. It thus prohibits dealers who have engaged in certain activities—albeit, activities with a First Amendment nexus, the giving of campaign contributions—from engaging in business with government entities where they might improperly benefit from what would otherwise be lawful, First Amendment protected activity.[15]

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[15] The fact that the subject, purpose and focus of the restriction is commercial market activity does not, of course, totally remove the matter from First Amendment scrutiny. But this is not the type of sensitive case in which the government has purposefully intervened in the First Amendment "marketplace of ideas" in an effort somehow to correct or regulate the way that marketplace functions. Such efforts to meddle with the flow of ideas strike near the core of First Amendment concern; though, in connection with political contributions, some such efforts have been sustained. *E.g., Buckley*, 424 U.S. at 24-29. In cases like this, where the restriction in question is squarely premised on the need to regulate a commercial marketplace, rather than a direct governmental effort to tamper with the principle of free and open exchange of ideas, First Amendment concerns are less pronounced.

The First Amendment conduct upon which the Rule has an impact is solely the giving of money to, and soliciting of money for, public officials. Such conduct has long been understood as a proper subject of government regulation. As this Court has recognized, giving money directly to candidates, even for ostensibly political purposes, represents First Amendment activity of a particularly modest sort. *E.g.*, *Buckley*, 424 U.S. at 20-21; *FEC v. National Right to Work Comm.*, 459 U.S. 197, 206-08 (1982) ("*NRWC*"). The Rule's bar against doing business with an issuer is triggered only when the dealer (or one of its municipal finance professionals or political action cc ittees) has made contributions to an official of that And the solicitation prohibition applies only to th citation of contributions to officials of issuers with who the dealer does or seeks to do business. The dealer or municipal finance professional remains free to speak directly on any political issue, to use his or her money to disseminate his or her political views, or even to support the same political candidate through independent expenditures in support of the candidacy. The limitation arises solely from efforts to provide money directly to the candidate or official with whom the dealer does or seeks to do business. Petitioner does not, of course, suggest that the First Amendment shields from government scrutiny the giving of money to government officials for corrupt purposes. To the contrary, it has long been understood that where the giving of money to public officials is concerned, the boundary between benign political activity and ethically questionable activity is often difficult to identify, creating a role for government in establishing the ground rules. Rule G-37 follows a long line of First Amendment precedent allowing for curbs on the flow of money to political candidates to prevent corruption, the appearance of corruption, and corrupting and coercive influence.

Thus, in *Buckley*, the Court upheld as constitutional FECA's limits on individual contributions to candidates,

but struck down limitations on independent expenditures made by individuals. *See FEC v. National Conservative Political Action Comm.*, 470 U.S. 480, 491 (1985) (describing the *Buckley* holding). The Court in *Buckley* began its analysis by reaffirming the principle that " '[n]either the right to associate nor the right to participate in political activities is absolute.' " 424 U.S. at 25 (quoting *Letter Carriers*, 413 U.S. at 567). In upholding FECA's limitation on contributions,[16] the Court recognized that such limitations represent "*only a marginal restriction upon the contributor's ability to engage in free communication*," and that the limitations do "*not in any way infringe the contributor's freedom to discuss candidates and issues.*" *Id.* at 20-21 (emphasis added). The Court held that the "marginal restriction" represented by contribution limitations was justified by "the prevention of corruption and the appearance of corruption spawned by the real or imagined coercive influence of large financial contributions on candidates' positions and on their actions if elected to office." *Id.* at 25.

This Court has also upheld FECA's restrictions on corporations and labor unions from *soliciting* campaign contributions. *NRWC*, 459 U.S. 197.[17] In upholding these provisions, the Court recognized that like contributions themselves, soliciting and coordinating contributions represent a modest form of First Amendment activity, and that contributions and solicitations of contributions by these particular industries or entities pose special risks to the political process. *Id.* at 206-11.[18]

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[16] The contribution restrictions prohibited individuals from contributing more than $25,000 in a single year or more than $1,000 to any single candidate for an election campaign. 424 U.S. at 13.

[17] Corporations and labor unions are prohibited from making contributions. The Act permits these entities to participate in limited soliciting, but only through a separate, segregated fund, established pursuant to and registered under FECA. *See* 2 U.S.C. § 441b.

[18] *See also United States v. Boyle*, 482 F.2d 755 (D.C. Cir.) (rejecting First Amendment challenge to FECA provisions regu-

The Court has also sustained the Hatch Act's total prohibition against federal employees—and against state and local employees engaged in activities financed in whole or in part by federal funds—from taking *any* part in political activities. *Letter Carriers*, 413 U.S. 548; *Oklahoma v. United States Civil Service Comm'n*, 330 U.S. 127 (1947). The Court held these provisions were justified both to ensure that government service "depend[s] upon meritorious performance rather than political service" (*Letter Carriers*, 413 U.S. at 557), and to protect government employees "from express or tacit invitation to . . . perform political chores in order to curry favor with their superiors rather than to act out their own beliefs . . . ." (*id.* at 566).[19]

5. Petitioner's effort to enlist *Buckley* in aid of his own cause does not withstand even the most superficial scrutiny. Petitioner bases his argument on that portion of *Buckley* which struck down FECA's limitations on *independent expenditures*, and all but ignores that portion of *Buckley* upholding FECA's restrictions on campaign *contributions*. *See* Petition at 11-13. This Court has consistently distinguished campaign contributions—which are controlled or coordinated by the candidate or campaign—from independent expenditures, which are not. The Court has just as consistently held that "restrictions on contributions require less compelling justification than restrictions on independent spending." *FEC v. Massachusetts Citizens for Life, Inc.*, 479 U.S. 238, 261 (1986) (citing *FEC v. National Conservative Political Action Comm.*, 470 U.S. 480 (1985); *California Medical Ass'n v. FEC*, 453 U.S. 182, 194, 196-97 (1981); *Buckley v. Valeo*,

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lating political contributions by labor unions), *cert. denied*, 414 U.S. 1076 (1973). FECA also bans the making and soliciting of contributions by government contractors. 2 U.S.C. § 441c.

[19] All fifty states have restricted the political activities of their own employees. *See Broadrick v. Oklahoma*, 413 U.S. 601, 604 n.2 (1973) (rejecting First Amendment challenge to Oklahoma's bar against state employees soliciting campaign contributions).

424 U.S. at 20-22). And, consistent with *Buckley* and these other precedents, Rule G-37 imposes *no* restrictions whatsoever on independent expenditures (and only indirectly affects contributions). Petitioner's focus on that part of *Buckley* dealing with independent expenditures is therefore inexplicable.

6. Nothwithstanding petitioner's effort to characterize Rule G-37 as a broad First Amendment intrusion, the rule concerns itself only with a narrow issue: giving or soliciting money to candidates and public officials in a position to employ public office to influence the grant of particularized benefits—lucrative municipal securities contracts—to the giver. The Rule does not even limit the giving of money directly to candidates in connection with state and municipal elections, if the dealer is *not* seeking to obtain business from the states or localities of those candidates. Indeed, even where the dealer has given or solicited a contribution to a municipal official, the Rule is narrowly drawn to apply only to transactions in which the possibility of the contribution influencing a governmental decision to award a municipal securities contract is real and palpable: the Rule does not apply to contracts that are awarded through a competitive bid process.

More important, the Rule has no application to the expression of opinion on public issues by dealers or municipal finance professionals, including expressions of opinion on the issues in a municipal election. It in no way prevents them from speaking out about the candidates directly, publicly, forcefully and vigorously. It in no way prevents them from spending as much money as they want in support of particular issues, viewpoints or candidates (so long as the expenditures are neither controlled nor coordinated by the candidate or campaign). The Rule addresses the potential for corruption only with a particular form of action, giving money to or soliciting money for the candidate from whom business is sought.[20]

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[20] Petitioner asserts that the Rule's restrictions affect "countless numbers of private citiens." Petition at 11. They do not. In

7. While conceding that the government would have an interest in punishing corrupt *quid pro quos*, petitioner argues that a prophylactic rule like this can only be justified by specific evidence that such *quid pro quo* arrangements are rampant in the municipal securities business. (Petitioner ignores the numerous complaints and reports concerning *quid pro quos* in the record.)

As recognized in *Buckley* and its progeny, however, the government may have a compelling interest in eliminating the *risk* and *appearance* of corruption through the adoption of sustainable *prophylactic* measures. To repeatedly assert (as petitioner does) that the record contains no hard evidence of specific *quid pro quos* is to misstate or misunderstand these precedents—as well as the purpose and justification of Rule G-37.

As the Court said of *quid pro quo* arrangements in *Buckley*, "the scope of such pernicious practices can never be reliably ascertained." 424 U.S. at 27. Thus, it is the "*potential*" for corruption "that demands regulation." *Austin v. Michigan State Chamber of Commerce*, 494 U.S. 652, 661 (1990) (emphasis added) (quoting *NRWC*, 459 U.S. at 209-10). The "*prevention* of corruption and the *appearance* of corruption spawned by the real *or imagined* coercive influence" of contributions are sufficient to warrant regulation. *Buckley*, 424 U.S. at 25 (emphasis added). Courts will not "second-guess a legislative determination as to the need for *prophylactic measures* where corruption is the evil feared." *NRWC*, 459 U.S. at 210 (emphasis added). *See also id.* at 208 (it is important to prevent "the eroding of public confidence . . . through *the appearance* of corruption") (emphasis added).

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comparison to the FECA and Hatch Act restrictions sustained by this Court, Rule G-37's restrictions affect a very small number of people: dealers and municipal finance professionals seeking to do business with issuers to whose officials they have made or solicited contributions.

While the governmental interests supporting the contribution and solicitation restrictions of FECA and the Hatch Act are broad and general—the need to safeguard the political process as a whole against unspecified forms of undue influence and political corruption—the governmental interest supporting Rule G-37 is quite narrow and specific. It is tied to the special relationship between dealers and issuer officials, where, in the absence of regulations, these dealers can do or seek to do business with the same officials to whom they have made direct payments in the form of campaign contributions, or for whom they have solicited contributions. (In other settings, similar conduct might be regarded as a "kickback.") The risk and appearance of corruption are clearly inherent in that relationship.

8. Petitioner's argument that even if the business prohibition is necessary, the solicitation restriction is not, was also properly rejected by the District of Columbia Circuit. As both commentors to the MSRB's original draft rule and the District of Columbia Circuit recognized, the business prohibition would be easily evaded if dealers or their municipal finance professionals could simply solicit or coordinate contributions instead. *See Blount*, 61 F.3d at 947. Not unlike FECA's "total" contribution limits, the solicitation prohibition "serves to prevent evasion" of the contribution restrictions by a person who is in the position to solicit or coordinate the giving of "massive amounts of money to a particular candidate . . . ." *Cf. Buckley*, 424 U.S. at 38.

9. Finally, the District of Columbia Circuit properly rejected petitioner's argument that there are less restrictive means available to further Rule G-37's goals—specifically the disclosure and record-keeping requirements instituted in Rule G-37(e) and Rules G-8 and G-9. As in *Buckley*, the government "was surely entitled to conclude that disclosure was only a partial measure." 424 U.S. at 28. Disclosure and record-keeping are especially unlikely to protect the market from the risk and appear-

ance of corruption within the specific context of pay-to-play. This is because in pay-to-play, contributions or solicitations are not exchanged for guaranteed business, but merely for being considered for business (thus making it difficult to specifically link the *quid* to the *quo; see Blount*, 61 F.3d at 945). Indeed, in the absence of contribution and solicitation provisions, disclosure may actually make the pay-to-play situation worse: in a regime where dealers believe they have to give or solicit contributions to be considered for business, disclosures of which dealer gave how much money to whom is likely to spur competition of the most unseemly kind, where one dealer tries to "one-up" the next by giving or soliciting more.

In sum, the District of Columbia Circuit properly applied this Court's well-established precedent in concluding that Rule G-37's indirect effect on the extent to which dealers will make or solicit contributions does not impermissibly infringe upon First Amendment rights. There is no need for this Court to revisit that determination.

II. THE DISTRICT OF COLUMBIA CIRCUIT PROPERLY REJECTED PETITIONER'S TENTH AMENDMENT CHALLENGE.

Petitioner's argument that Rule G-37 violates the Tenth Amendment is thus premised on a fundamental misconception of what Rule G-37 does. As the Court of Appeals recognized, Rule G-37 does what all MSRB rules do and are supposed to do: they regulate the activities of dealers engaged in interstate commerce. That the Rule has an ancillary effect on state and local elections is insufficient to implicate the Tenth Amendment. Countless federal regulations indirectly affect states and localities—and any regulation of the market in municipal securities has an impact on municipal governments. But this does not mean they encroach on the powers of *state government* in a way that violates the Tenth Amendment.

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In *Oklahoma v. United States Civil Service Commission*, 330 U.S. 127, 142-44 (1947), this Court rejected a Tenth Amendment (as well as a First Amendment) challenge to that part of the Hatch Act which precludes state and local officials employed in activity funded in whole or in part by the United States from participating in any political activities. The Court held that "[w]hile the United States is not concerned with, and has no power to regulate, local political activities as such of state officials, it does have power to fix the terms upon which its money allotments to states shall be distributed." *Id.* at 143. The Court continued: "the Tenth Amendment has consistently been construed 'as not depriving the national government of authority to resort to all means for the exercise of a granted power which are appropriate and plainly adapted to the permitted end.'" *Id.* (quoting *United States v. Darby*, 312 U.S. 100, 124 (1941)).

Even more clearly, the federal government has the power to fix the terms on which dealers engaged in interstate commerce conduct their business. In the words of the Court of Appeals, petitioner "points to no theory of the Tenth Amendment or the commerce clause under which Congress [or an agency acting at the direction of Congress, *see, e.g., North American Co. v. SEC*, 327 U.S. 686 (1946)] is disabled from regulating private persons in their conduct of interstate trade in municipal securities." *Blount*, 61 F.3d 949.

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CONCLUSION

For the foregoing reasons, the MSRB respectfully submits that the Petition should be denied.

Respectfully submitted,

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